

BOARD OF INVESTMENT TRUSTEES

MONTGOMERY COUNTY EMPLOYEE RETIREMENT PLANS



SERVICE PROVIDER PROCUREMENT POLICY

BOARD OF INVESTMENT TRUSTEES

SERVICE PROVIDER PROCUREMENT POLICY

Table of Contents

	Page
I. <u>Purpose & Authorities</u>	
A. Purpose of Policy Statement/Board Requirements	1
B. Statutory Board Responsibility and Authority to Contract for Services	1
C. Board Exemption from County Procurement Regulations	1
D. Communications Responsibilities	1
II. <u>Procurement of Services – Procedures</u>	
A. Stage 1- ERP Program Requirements	1
B. Stage 2 - Research process	2
1. Criteria	2
2. Candidate sources	2
3. Minority Participation	2
4. Selection of Candidates-Issuance of Request for Information	2
C. Stage 3 - Review and Verification Process	3
1. Due diligence evaluations	3
2. Selection of finalists	3
3. Contracting	3
D. Stage 4 - Selection of Finalist and Contract Process	4
1. Vote	4
2. Contract process and negotiations	4
3. Contract execution	4
III. <u>Monitoring of Contractors</u>	
A. Review Process	4
B. Contract Modifications	5
IV. <u>Termination of Service Provider</u>	
A. Basis for termination	5
B. Procedures	5
V. <u>Records Retention</u>	5
VI. <u>Ethics</u>	6
VII. <u>Policy Review</u>	6
VIII. <u>Appendix A</u> – Search criteria for the procurement of investment advisor services	7

BOARD OF INVESTMENT TRUSTEES
SERVICE PROVIDER PROCUREMENT POLICY

I. Purpose & Authorities

A. Purpose of Policy Statement/Board Requirements

The purpose of this statement is to define the policy of the Board of Investment Trustees (the “Board”) regarding the procurement of external service providers. These services are required in the management of the investment programs for the Employee Retirement Plans (the “ERP”) for which the Board is responsible. The policy statement is a guideline for the Board’s procurement process, which is intended to foster competition and fairness while being flexible to meet the needs of a dynamic investment environment.

This policy does not cover procurement of Board office administrative services, which generally follows established County contracts and procedures (i.e., procurement of supplies, mini-contracts, etc.)

B. Statutory Board Responsibility and Authority to Contract for Services

Pursuant to Section 33-60 of the Montgomery County Code, the Board has the fiduciary responsibility for the governance of the ERP investment management programs and has exclusive authority to contract for services to meet this responsibility.

C. Board Exemption from County Procurement Regulations

Pursuant to Section 33-60 of the Montgomery County Code, the Board is exempt from the Montgomery County Government procurement regulations in the procurement of services for the management of ERP assets. However, as specified in this statement of policy, the Board adheres to a competitive procurement process in the procurement of investment advisory services.

D. Communications Responsibilities

Official communications related to Board procurement processes and activities will be coordinated by Board staff. Staff will report items of significance to the Board as appropriate.

II. Procurement of Services - Procedures

A. Stage 1 – ERP Program requirements

- The Investment Committee or Administrative Committee will recommend to the Board the services necessary to meet the goals of the program, including:
 - Hiring/Terminating of service providers
 - Number of service providers sought
 - Urgency/timeframe for search
 - Consultant support required

B. Stage 2 – Research Process

This stage involves determining search criteria and sources and the list of possible candidates that may meet Board needs as specified in Stage 1.

1. Criteria

Appendix A documents specific search criteria typically used for the selection of investment managers for the ERP. The Board or the appropriate Committee may add additional criteria to be used in a particular search.

2. Candidate sources

Although not limited to the sources indicated below, staff will generally use these sources to identify eligible candidates. Staff may also use sources identified by the Board's consultant. The Board or the appropriate Committee may recommend additional sources to be used in a particular search.

- Consultants' data bases including but not limited to:
 - Board consultant data base
 - Software databases provided by other vendor(s)
- Industry reports, newspapers, newsletters and articles
- Marketing materials received by Board office
- Plan sponsor and plan sponsor contacts
- Reports and sources used to identify minority-, female-, and disabled-owned firms (MFD)
- Montgomery County resources and information

3. Minority Participation

The Board, staff and consultants are committed to including minority-, female-, and disabled-owned firms (MFD firms) among prospective service provider candidates. Special efforts made to ensure identification of possible eligible firms in the search process include:

- regular monitoring of above-referenced sources to identify possible candidates
- regular review of service providers utilizing MFD firms
- staff interviews with MFD firms on an ongoing basis
- maintenance of research files on such firms to assist efforts when searches begin

4. Selection of Candidates-Issuance of Request For Information

Based on criteria and sources noted above, staff will prepare a list of possible candidates for a specific search. Staff, with the assistance of the investment consultant, will issue a Request For Information to the candidates selected.

C. Stage 3 – Review and Verification Process

Stage 3 of the search process focuses on review and verification of information pertaining to the list of candidates identified in Stage 2. Completion of the Stage 3 process should result in the selection of a finalist.

1. Due diligence evaluations

Staff will complete a due diligence process to confirm findings identified in Stage 2. Those candidates deemed to be eligible will be interviewed by staff by phone or in person in the Board's office. The results of the interviews, and recommendation of semi-finalists, will be presented to the appropriate Committee. A summary of the candidate's evaluation prepared by staff will include but is not limited to:

- Quantitative information resulting from Stage 2 criteria.
- Qualitative information related to candidate's experience, strategies and operations including:
 - organizational structure
 - experience and depth of personnel, including turnover
 - firm-specific operational philosophy
 - fees
 - references from Board consultant(s)
 - references from other sources
 - in the case of limited partnership arrangements such as real estate funds, fund-specific aspects including but not limited to liquidity and tax issues.
 - firm-specific legal/litigation issues

2. Selection of finalists

Staff will report due diligence information to the appropriate Committee and present no more than 4 candidates for consideration to the appropriate Committee. The Board's consultant will review and comment if appropriate. The Committee will interview the candidates and recommend a finalist(s) to the Board. The selection of the finalist(s) will be based on both quantitative and qualitative evaluations as well as interviews.

3. After the Committee has selected a finalist(s), Staff will ensure that there are no issues with the vendor to prohibit the Board from entering into a contract.

D. Stage 4 – Selection of Finalist(s) and Contract Process

The Board will vote on the Committee's recommendation of a service provider(s) at a meeting of the Board pursuant to Board bylaws. Staff, in conjunction with its General Counsel, will handle the contract process.

1. Vote

The Board will vote based on all information made available by the Committee, including information on the entire search process as summarized by staff, subsequent materials prepared for Board consideration, final interviews and due diligence meetings if held. The Board will vote by formal resolution.

If the Board does not vote to accept the Committee's recommendation, then the Board will determine at what stage to recommence the procurement process.

2. Contract process and negotiations

Staff will pursue contract negotiations, including terms related to fees, operational issues and guidelines, and will apprise the appropriate Committee if needed.

A. Separate account agreements may follow a format approved by the Committee and will include provisions for:

- establishment of the account and assignment of management and fiduciary responsibility if required
- directions pertaining to the operations of the account
- directions pertaining to Board and staff authorities and communications
- determination of professional liability insurance for errors and omissions
- establishment of fee and terms of invoicing and payment
- contract termination upon notice by either Board or service provider
- delivery of any other federal or state regulatory required disclosures prior to contract execution
- County-required specifications related to nondiscrimination in contracting and ethics rules
- addenda related to Board policies and procedures, and operational guidelines

B. All service provider agreements will be reviewed by staff and the Board's legal counsel to confirm conformance with Board policies and authorities.

3. Contract execution

All agreements and contracts will be approved and executed in accordance with Board bylaws and signature authorities specified in Board resolutions.

III. Monitoring of Contractors

A. Review process

Staff will conduct contract compliance reviews on an ongoing basis, including reviews of service provider performance, conformance to guidelines, organizational structure and any other performance requirements as specified in the service provider's contract. Beyond performance and contract compliance matters, contractor-related matters will be reported to the Board when deemed significant, i.e. if the matter(s) have a possible effect on the service provider's ability to perform as expected. The appropriate Committee will review compliance issues and make recommendations to the Board if appropriate.

Annually staff will conduct reviews of all aspects of the service provider's contract. The review may include a due diligence review in the service provider's office or the Board's office when necessary. Matters to be reviewed include but are not limited to the quantitative and qualitative factors which served as the basis for selection as a service provider. The appropriate Committee will report to the Board on the results of the annual review of all service providers.

B. Contract modifications

Staff will advise the Board of any suggested modifications to the contract terms, including service provider ownership changes whether requested by the service provider or by staff. Staff, with the assistance of legal counsel, will determine the appropriate method of modification, i.e. contract amendment or letter agreement. Staff will recommend an approval method and background information required by the Board to consider any such modification. Staff will also provide a recommendation regarding the modification for Board consideration. Pursuant to Board bylaws, the Board will approve contract modifications through resolution which will be implemented by staff.

IV. Termination of service providers

A. Basis for termination

The Board may terminate a service provider at any time. Contract terms must provide for immediate termination upon written notice by the Board. The Board may terminate service providers for any reason, including but not limited to one or more of the following reasons:

- ERP program changes
- Underachievement of performance expectations as set forth in (i) operating guidelines incorporated into the agreements and (ii) review procedures specified in Section III above
- Contractor-specific issues related to lack of adherence to contract terms or guidelines, change in organization or personnel, fees, or any other changes in the service provider's business strategies.

B. Procedures

Staff will provide background information regarding any basis for termination of a service provider. The appropriate Committee will consider such information and will make a recommendation regarding Board action. If the termination is a matter of urgency, staff will recommend consideration by the Board. Action to terminate a service provider must be by resolution. Staff will determine and implement the appropriate account transfer/liquidation procedures, informing the Board as necessary.

V. Records Retention

Staff will maintain service provider records in the Board office throughout the duration of the service provider relationship. Service provider records will include search-related materials presented to the Board at the time of selection as well as legal and correspondence files. Records

will be retained in accordance with Board office procedures. Records will be archived in accordance with the Board office's records retention policy.

VI. Ethics

The Board, and staff, will at all times conform to County ethics laws, rules and regulations related to procurement and involvement with contractors. In addition to County ethics laws, rules and regulations, individual Board and staff members will disclose to the Board any inherent or potential conflicts of interest in dealing with specific service providers prior to taking any official action concerning any service provider.

The Board will be notified of any violation of County or Board ethics rules by any Board or staff member and will handle ethics issues in accordance with County Government procedures. The Administrative Committee of the Board will be responsible for monitoring adherence to this section of the Board's procurement policy.

VI. Policy Review

This policy will be reviewed and amendments recommended by the Administrative Committee.

Appendix A

Search criteria for the procurement of investment advisor services

A. Specification of needs

When the Board has determined the need for investment management services, it will make changes that are deemed appropriate based on the analysis of a plan's risk and return profile. Changes are expected to improve the risk adjusted return. Specific investment advisor contracting needs required to accomplish the effective management of the Plans will be at the sole discretion of the Board.

B. Criteria to be used for Investment Advisors procurements

Based on style specific needs, staff will recommend a list of criteria for determining eligible candidates. The initial criteria will pertain to minimum requirements related to investment management experience in the specific style sought by the Board:

- a. style parameters based on fundamental characteristics of sample portfolio, e.g., average market cap, P/E, EPS growth rate, duration, industry/sector exposure, etc., and return-based regression analysis; or, fund characteristics, including but not limited to fund type and property diversification in the case of real estate funds
- b. years in business (minimum 3 years for firm or product unless waived by Board or Investment Committee)
- c. assets under management (minimum \$100 million, with at least \$40 million in product, unless waived by the Board or Investment Committee)
- d. investment performance (minimum performance requirements include index-like return net-of-fees in asset class for trailing 3 to 5 year periods, and above median performance in investment advisor peer comparisons for trailing 3 year periods)

C. Due diligence review by staff

As part of the processes as outlined in the Section D of Service Provider Procurement Policy, staff will perform on site due diligence reviews of managers at their location. The review will cover the following items:

- people and organization of the firm
- philosophy and process of investment strategy
- resources dedicated to the investment strategy
- performance of the product that is being reviewed

Along with this review, staff will prepare a written report following the outline as shown in Attachment 1. This form may also be used for monitoring purposes of existing investment advisors, whenever a visit is performed by staff.

Attachment 1
Due Diligence Outline for Manager Evaluation

Firm:
Evaluation by:
Onsite visit: ☐yes ☐no

Product Type:
Date of Evaluation:

People/Organization	Scoring	Score	Comments
	0-100		
Ownership/Incentives <ul style="list-style-type: none"> • Direct Ownership • Phantom Stock • Profit-sharing • Performance Bonus • Depth of Incentives 	Total 0- 25 20 15 10 5 0-5		
Assets Under Management <ul style="list-style-type: none"> • Firm-wide growth of assets • Continuity of product lines 	Total 0-10 5 5		
Team <ul style="list-style-type: none"> • Communication Links • Role of Professionals • Research • Operations 	Total 0-20 5 5 5 5		
Quality of Key Professionals <ul style="list-style-type: none"> • Quality of Leadership and Motivation • Experience(years in Industry/ with the firm/ on the team) • Quality of Education and ongoing education 	Total 0- 15 5 5 5		
Turnover of Senior professionals (3 years) <ul style="list-style-type: none"> • None • Low (<10%) • Medium (<20%) • High (>20%) 	Total 0-15 15 10 5 0		
Commitment to Improvement <ul style="list-style-type: none"> • Clear mission Statement/ Business plans • Reinvestment • Process Enhancement/ Improvements 	Total 0-15 5 5 5		

Philosophy/Process	Scoring	Score	Comments
	0-100		
Market Anomaly/Inefficiency <ul style="list-style-type: none"> • Clear Identification • Permanent or Temporary 	Total 0-30		
Information <ul style="list-style-type: none"> • Unique Sources • Unique Processing 	Total 0-10		
Buy/Sell Disciplines	Total 0-15		
Portfolio Construction <ul style="list-style-type: none"> • Benchmark Orientation • Risk Controls 	Total 0-20		
Quality Control <ul style="list-style-type: none"> • Return Consistency • Style Consistency • Performance Attribution 	Total 0-15		
Assets Under Management <ul style="list-style-type: none"> • Level of product assets not restrictive of overall strategy • Capacity constraint • Asset growth/decline 	Total 0-10		
Resources			
	0-100		
Research (Alpha Generation)	Total 0-40		
Information Systems Management	Total 0-15		
Marketing/Client Service/Administration/Backoffice	Total 0-15		
Trading <ul style="list-style-type: none"> • Turnover Relative to Process • Sophistication of Trading Process (# of independent traders, experience of traders, systems) • Measurement of Trading Costs 	Total 0-30 10 15 5		
Performance			
Risk-Adjusted Returns <ul style="list-style-type: none"> • Relative to Benchmark • Relative to Peer Group 	Total 0-100 0-30 0-70		
Fees	Calculated		

Other Notes on the Manager and Conclusions